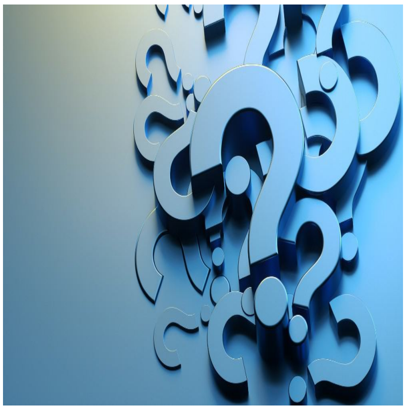

Which Canadian Bank Stock Is the Most Undervalued?

Description

Canadian banks continue to hover around in limbo after shares got battered in the vicious February-March coronavirus crash. While the **TSX Index** and U.S. markets have mostly recovered from the unprecedented implosion in stock prices, many of the big banks have barely budged.

In unprecedented economic shocks, the pressures tend to fall all the way back to the banks. While it seems like the big banks aren't going to participate in the broader market relief rally this time around, it's worth considering that the big banks typically come out of the gate surging on the back of a new bull market.

Canadian bank stocks are under pressure

The Canadian banks have been hit with a perfect storm of headwinds. It's not just the coronavirus crisis that has wreaked havoc on various sectors of the Canadian economy. There's also the rare nationwide credit downturn they've been facing over the past few years. Short-sellers targeted the big Canadian banks because of the credit downturn well before there was any chance we'd fall into a pandemic, noting that many of the big banks were ill-prepared to deal with such a tightening of credit.

Today, the banks are in a tough spot, with provisions for loan losses steepening and less loan growth expected at lower margins. Near-zero interest rates are thinning out already razor-thin net interest margins (NIMs). With nothing to get excited about, most Canadians have thrown in the towel on Canada's Big Six banks, despite their impressive dividend-growth track records.

Sure, the banks look like duds. And they will probably trail any meaningful rally in the broader markets. But for those with a long-term horizon, I think there's an opportunity to be had at these depths. To beat the markets, you need to be an aggressive buyer of stocks that nobody else wants. And with the banks continuing to tread water, I think now is a great time to lock in slightly higher-than-average dividend yields alongside valuations that haven't been this depressed since the Financial Crisis.

Given the Big Six Canadian banks have been tested for stress time and time again, they're on much more stable footing than they were just over a dozen years ago. As such, I believe many Canadian banks are ripe for picking right now.

TD Bank is a premium bank stock at a not-so-premium price

And at the top of my shopping list is **TD Bank** (TSX:TD)(NYSE:TD), a premier banking stock that's no longer trading at a premium price tag. The management team has a knack for mitigating risks without compromising on the return front. While provisions have undoubtedly gotten a bit out of hand, it's important to note that even though the bank's risk-management abilities are top notch, the bank couldn't navigate arguably the worst shock this economy has been hit with.

The Financial Crisis saw TD and its Canadian bank peers get caught with their pants down, but they were relatively quick to recover after the dust had a chance to settle, despite their relatively mediocre capital positions. Today, TD is well capitalized and better positioned to weather the storm. The only difference is that the coronavirus crisis came quickly, blindsiding most firms and giving them no time to prepare for the damage to come.

Had this recession been more structural and gradual in nature, I'm sure TD stock would not have crashed so sharply, and management would have been able to dampen some of the downside. But given the coronavirus shock hit in what seemed to be an instant, TD wasn't able to mitigate the risks that it was suddenly served up.

While TD could have done a better job of mitigating risks associated with its U.S. business, I think it's a mistake to believe that TD had suddenly lost its risk-management advantage overnight. As such, investors looking for a premium long-term holding ought to consider backing up the truck on shares today while they're trading at around 1.2 times book.

Foolish takeaway on TD Bank

TD isn't a risky regional bank that's at risk of losing control amid this crisis. But the current valuation may be suggestive of such. So, stash the name in your TFSA and collect the 5.1%-yielding dividend.

While there are cheaper Canadian bank stocks based on traditional valuation metrics, I think that relative to the calibre of business, TD Bank is the best bank for your buck.

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joefrenette